

## General

This section provides an overview of the accounting principles and basis of accounting for this accounting manual. By presenting a summary of this information in advance of the examination of the expenditure, revenue, and general ledger accounts, the knowledge of these guidelines will help to establish a system philosophy applicable to this accounting manual.

## Basis of Accounting

The “basis of accounting” refers to the point in time when revenues, expenditures or expenses (as appropriate), and the related assets and liabilities are recognized in the accounts and reported in the financial statements. School districts in Missouri typically operate under the cash, modified cash or modified accrual basis of accounting.

## Cash Accounting

The cash basis of accounting is the most elementary form of accounting and is typically used by individuals, small businesses, and school districts. Under the cash basis, revenues are recorded when received and expenditures are recorded when monies are paid.

The virtue of cash accounting is its simplicity. As accounting is not performed until monies are received or spent, the relationship of revenues and expenses to the accounting period in question is dependent on the actual flow of cash. This system makes no provision for noncash transactions; therefore, the accounting reports may provide inadequate information for control purposes and may limit analysis of the financial condition of the entity.

The modified cash basis of accounting is the cash basis of accounting that incorporates modifications “having substantial support.” A modification having substantial support is not clearly defined. However, these modifications are frequently to recognize certain transactions on an accrual basis and, thereby, represent transactions that would be reported by an entity following GAAP. The modifications should also not be considered illogical (e.g., recognizing revenues on the accrual basis and expenses on the cash basis). Districts need to work with their independent auditors to resolve any questions or issues relating to the modified cash basis of accounting.

## Accrual Accounting

Accrual accounting is a system whereby revenues are recognized when earned and expenditures are recognized in the period incurred, without regard to the time of receipt or payment of cash. This method of accounting allows a more accurate evaluation of operations during a given fiscal period. Accrual accounting may be based on one of two methods: full accrual or modified accrual.

The term “full accrual” is sometimes employed and can have one of two meanings. Either an extensive number of categories in both revenues and expenditures are accrued and/or this activity is continuous (daily) rather than periodic. Increasing the degree of complexity of financial reporting creates an associated cost in the posting, recording, and balancing of more accounts. Full accrual is typically used in enterprise and agency funds as a number of major items that are considered expenses in a full costing system (such as depreciation) need to be recognized.

Modified accrual accounting falls between the cash basis and the full accrual basis and is the most common accrual basis used by school districts. In modified accrual accounting, most items of revenue and expenditures may be handled on a “cash” basis for daily processing and converted to an accrual basis by periodic adjustments. The determination of how frequently the adjustments will be made is a value judgment that depends on the significance of the items, the purposes for the accounting, the need to reflect the operations of the enterprise, and the associated cost and complexity of the system.

Since the resulting reports are produced at the end of an accounting period, some adjustments can best be made as they happen (daily) and others only at the end of the accounting period.

The primary components of any accounting system are:

- properly matching the revenues and expenditures of an accounting period
- properly comparing actual revenues to budgeted revenues of an accounting period
- properly comparing actual expenditures to budgeted expenditures of an accounting period

### Single-Entry Accounting System

The check register in a checkbook easily illustrates a single-entry accounting system. In that system, a single entry is recorded for each cash receipt or cash disbursement. The cash account is increased or decreased by each transaction. Single-entry accounting systems in LEAs operate in a similar manner.

### Double-Entry Accounting System

For the proper recording, balancing, and control of accounting transactions, every LEA **shall** employ the double-entry accounting system. Such systems may be on a cash basis and nothing herein shall be construed as requiring any school district to change from a cash basis of accounting. The principle of the double-entry accounting system is that for every entry made to the debit side of a fund account or accounts, an entry or entries for a corresponding amount will be made to the credit side of an account or accounts for the same funds. The debits must always equal the credits.

### Rules of Debit and Credit for Double-Entry Accounting Systems

Assets		=	Liabilities		+	Fund Balance	
Debit for Increase	Credit for Decrease		Debit for Decrease	Credit for Increase		Debit for Decrease	Credit for Increase

  

Revenues			Expenses	
Debit for Decrease	Credit for Increase		Debit for Increase	Credit for Decrease

### Normal Fund Balances

Assets	-	Debit
Liabilities	-	Credit
Fund Balance	-	Credit
Revenues	-	Credit
Expenses	-	Debit

### Daily Adjustments

Daily adjustments are primarily related to cash disbursements and cash receipts. It is recommended that these adjustments be made daily for the simple reason that it is easier to maintain control of these adjustments if done continuously. No additional work is involved in performing this activity as the transactions occur. The major types of adjustments on a daily basis include investments, inventory, cash advances, and encumbrances.

### Investments

A purchase of an investment requires a disbursement of cash. This disbursement does not represent an expense of the organization but an exchange of one asset (cash) for another asset (investment). Redemption of the investment principal also does not represent income to the organization but merely an exchange of assets.

**Inventory**

A school district shall maintain an inventory system. The purchase of inventory is an exchange of assets, and should not be expensed or charged against the budget until it is shipped from the central warehouse to the organization requisitioning the item. If a district does not capitalize an inventory item, it should be expensed at the time of purchase.

**Cash Advances**

Cash advances are disbursements in advance of the actual expenditure and in themselves do not represent an expenditure. The expenditure occurs when the actual spending of the cash advance takes place.

**Encumbrances (Issuance of Purchase Orders)**

Encumbrances are contracts and other non-salary commitments that are evidenced by the issuance of a purchase order (see Section L: Encumbrance Accounting).

**End-of-Period Adjustments**

Certain other accrual adjustments to record revenue and expenditure items into the proper accounting period are required. These adjustments are not done daily but at the end of an accounting period.

The accounting period may be monthly for items included in monthly budgeted revenue and expenditure reports and annually for all others.

**Payrolls**

Payroll periods typically do not coincide with accounting periods. Therefore, at the end of the accounting period, some payroll expense will have accrued. An adjustment is required to allocate the payroll cost to the proper accounting period.

It is recommended that payrolls be accrued monthly as payroll costs amount to a substantial portion of any district's budget. Payrolls may be accrued on the basis of the daily pay rate. However, payrolls shall be accrued at year-end. Additionally, the district may need to accrue fringe benefits associated with the payroll.

Districts on a cash basis may accomplish the same result by writing payroll checks for the tenth through the twelfth month on June 30. Salary amounts earned but unpaid for the current fiscal year are recorded as expenditures as of that date. Individual payroll checks would then be distributed in the appropriate month. Cash flow and compliance with other statutory expenditure requirements may force a district to look carefully at how this procedure will impact the district (see Section L: Payroll).

**Prepays**

Certain costs are sometimes paid in advance. Per GASB, expenditures for insurance and other similar services extending over more than one accounting period need not be allocated between or among accounting periods, but may be accounted for as expenditures in the period of acquisition.

**Receivables**

Receivables represent items (revenues) recorded in the current accounting period that have not yet been received. The anticipated amount of current and delinquent property taxes to finance the budget of a particular fiscal period and the revenue produced from these taxes should be recognized in the fiscal period for which it was levied. The revenue must be due and receivable within the current period or expected to be collected soon enough thereafter to

be used to pay liabilities of the current period. Such time shall not exceed 60 days. If because of unusual circumstances, the facts justify a period greater than 60 days, the district should disclose the period being used and the facts that justify it (per GASB).

The following revenues should not be accrued:

- 5113 - School District Trust Fund (Proposition C)
- 5211 - Fines, Escheats, Overplus
- 5311 - Basic Formula
- 5312 - Transportation
- 5313 - Exceptional Pupil Aid
- 5315 - Remedial Reading
- 5316 - Gifted
- 5318 - Free and Reduced Lunch/At-Risk
- 5331 - Foreign Insurance Aid (Free Textbook)
- 5334 - Fair Share (Cigarette Tax)

### **Accounts Payable**

Accounts payable represent items (expenditures) charged to the current accounting period that have not been paid.

### **Reserve for Encumbrances**

This account is used for items properly charged to the current accounting period, but which are not paid or recognized as accounts payable as of the end of an accounting period (see Section L: Encumbrance Accounting).

### **Standard Costs (Internal Operations)**

There are several major areas where it is necessary and practical to attribute costs to the ultimate users (expense accounts or centers) even though the costs to the district for such goods and services have been commingled with other costs. This accounting technique (or cost proration) requires the establishment of a “price” to the user that will, in total for all users, reflect the user’s share of the total expense of the supporting activity. These include the following categories:

- Inventory - The initial cost of items held in inventory will provide a measure of expense allocation upon the issuance of supplies and materials from inventory to a specific using expense center.
- Printing (In-House) - This activity combines both direct material costs and labor services that should be charged to the using expense center as its fair share for goods and services rendered.
- Data Processing Services (Internal) - Districts that have their own electronic data processing (EDP) system will allocate costs for direct services to instructional activities so as to reflect these costs in the applicable programs (not administrative support).
- Maintenance and Repair Services - Direct and indirect maintenance costs should be charged to other programs such as keyboarding instruction for computer repair costs on instructional computers. Conversely, non-maintenance activities (such as vocational instruction) may incur costs that should be charged back to maintenance and operation for material or services performed.
- Construction and Remodeling - Costs incurred by a district that result in an addition to physical assets or a capital improvement must be charged to capital expenditures. These costs, such as those incurred by a carpenter shop to construct built-in storage, should result in increasing capital expenditures and reducing operating costs.